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SUBJECT: BRAZIL: UPDATES TO 2003 NTE

Ref: A) STATE 310953 B) JADAMS/LYANG EMAIL

¶1. Per Ref A, this cable transmits post's draft of the 2003 NTE. A separate copy is being emailed directly to USTR (Cronin and Blue).

IMPORT POLICIES

Brazil's arithmetic average applied tariff was an estimated 11.5 percent in 2003. Brazil currently maintains no applied tariff rates in excess of 35 percent, but does have safeguard measures in place for some imports, such as toys. For example, Brazil imposes tariffs between 4.5-16.5% on wood products and 22% on motorcycles. In April 2002, the Brazilian government approved a new tax law that dramatically increased the duty on imported advertising materials and discriminates between domestic and foreign producers. A number of imports are prohibited, including various used goods such as machinery, foreign blood products, refurbished medical equipment, automobiles, clothing, and other consumer goods.

Brazil and its MERCOSUR partners, Argentina, Paraguay and Uruguay, implemented the MERCOSUR Common External Tariff (CET) on January 1, 1995. The CET currently covers 9,626 items, with tariffs mostly ranging between zero and 21.5 percent. Within the CET, certain sectors are treated separately and are organized on special lists. The list for informatics and telecommunication goods contains 427 items with tariffs in 2002 ranging between zero and 26 percent; a tariff phase-down schedule should bring the top tariff down to 16 by 2006. The automotive list covers 55 items (vehicles and parts) with a tariff rate of 35 percent; Brazil has negotiated automotive agreements with third countries, which provide duty-free treatment within quotas. A MERCOSUR suspension of duties ranging from 2 to 15.5 percent on some 550 pharmaceutical products has been extended until December 31, 2003. Although the CET was meant to be a comprehensive, common tariff schedule, MERCOSUR countries have agreed to allow exceptions.

Brazil has 100 exceptions to the CET, with tariffs reaching as high as 55 percent on coconuts and peaches. In addition, after consulting with its MERCOSUR neighbors, in November 1997 Brazil implemented a temporary three-percentage point increase on most CET tariff items. For almost all products, this additional tariff was reduced to 1.5 percent by the end of 2002, with its total elimination expected at the end of 2003. Currently, 3450 CET items are excluded, including 1152 capital goods. The CET remains a significant barrier to increased U.S. exports of agricultural products, distilled spirits, and computer and telecommunications equipment. Brazil prohibits the importation of second hand consumer goods. In addition, significant barriers exist to U.S. textile exports. In particular, Brazil applies additional import taxes and charges that can effectively double the actual cost of importing textile products into Brazil.

Virtually all imports from its MERCOSUR partners enter Brazil duty-free. Notable exceptions are automobiles and automobile parts, which are subject to out-of-quota tariffs, and refined sugar, which is assessed a 17.5 percent tariff. Two-way trade between Brazil and its MERCOSUR partners increased by 25 percent during January to October 2003 compared with the same period a year earlier, evidence of continuing economic improvement that began in 2002. In a December 16, 2003 summit, MERCOSUR leaders reaffirmed their commitment to strengthen the customs union and work to fully integrate the MERCOSUR common market by 2006. MERCOSUR plans to finalize free-trade agreements with three Andean countries, Colombia, Venezuela, and Ecuador. Peru and Bolivia are currently associate members.

Import Licensing/Customs Valuation

The Secretariat of Foreign Trade (SECEX) implemented a computerized trade documentation system (SISCOMEX) in early 1997 to handle import licensing. All importers must register with SECEX to access SISCOMEX; registration requirements are onerous, including a minimum capital requirement. In addition, fees are assessed for each

import statement submitted through SISCOMEX. As a general rule, imports into Brazil fall within an "automatic import license" process. Originally, Brazil's non-automatic import licensing system was used only in cases of specific imports that require special authorization from specific ministries/agencies: beverages (Ministry of Agriculture); pharmaceuticals (Ministry of Health); arms and munitions (National Defense Ministry); etc. In 1998, the Brazilian government stopped publishing a list of products subject to non-automatic licenses; the only method available now for determining if a product requires an import license is to check the SISCOMEX system, which is available only to registered importers. Under Brazil's non-automatic import licensing system, U.S. suppliers have no means of finding out in advance which products require import licenses and whether they are subject to minimum price and payment terms as a condition of receiving a license.

Under Brazilian customs regulations, a "gray line" process exists for enhanced scrutiny of suspected fraudulent imports. This process is opaque and burdens some categories of U.S. exports. A related concern has been the possible use of the gray line process to impose minimum reference prices. In November 1999, the United States actively participated as an interested third party in EU WTO consultations on the issue, and in July 2000, the United States held its own WTO consultations with Brazil. The Brazilian Government denies the use of minimum reference prices and reportedly has modified its customs regime in response to these consultations.

Product registrations from the Ministry of Health are required for imported processed food products and food supplement products, and as of March 1, 2000, the term of validity for registration was shortened. Registration fees for these imports, as well as for medical and pharmaceutical products, have increased significantly. The U.S. Government also has received complaints relating to Brazilian practices that lead to non-transparent preferences for Brazilian products in procurement bids for government and nonprofit hospitals, and cause bias against the import of refurbished medical equipment when domestically produced "similar" exist. Implementation of such import measures continues to have a negative impact on U.S. exports, especially given the high tariffs on medical equipment. Although some progress in increasing the transparency of the process was made at the end of 2001, problems for U.S. exporters still exist. U.S. companies continue to complain of a variety of customs-related non-tariff barriers.

The U.S. Government has received complaints that the ICMS value-added tax collected by individual states is sometimes set to favor local companies, constituting a non-tariff trade barrier. Similarly, some U.S. companies have raised concerns about the arbitrary application of various non-automatic import licensing procedures, such as authorizations from the Federal Police and the Nuclear Regulatory Agency.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Sanitary and Phytosanitary Measures

Progress has been made in the area of sanitary and phytosanitary (SPS) measures. On March 15, 2001, the Ministry of Agriculture lifted the ban on U.S. Soft Red Winter, Hard Red Spring, and Hard Red Winter wheat shipped from non-west coast ports. The ban remains on Durum and White wheats and wheat from the states of Washington, Oregon, Idaho, California, Nevada, and Arizona due to phytosanitary concerns. The U.S. Government continues to work with the Brazilian government to resolve the remaining import restrictions.

Despite progress, SPS measures remain significant barriers in several cases. Brazil continues to prohibit the entry of poultry and poultry products from the United States based on an alleged lack of reciprocity, contrary to WTO rules which dictate that sanitary and phytosanitary determinations be based upon sufficient scientific evidence. Attempts to import seed potatoes into Brazil have been blocked by unresolved permit issues based upon a delayed and non-transparent pest risk assessment (PRA) before commercial market access is granted. Brazilian legislation also bans the importation of beef produced with growth hormones; however, beef imports from the United States have been allowed on a waiver basis since 1991.

Biotechnology

The biotechnology debate has captured public attention in Brazil with frequent and polemical reports in the press presenting various aspects of the issue. Regulation of the biotech sector remains essentially frozen because of a

1998 court case that is still pending in a federal court in Brasilia, filed by environmental NGOs against the use of Monsanto's Roundup Ready soybean variety. The case addresses not only the requirement to conduct environmental impact studies on GMO products, but also the constitutional authority of the Government's CTNBio commission to approve biotech products.

In the absence of a definitive court ruling on this case, President Lula made considerable progress in 2003 towards a new legal framework for production and marketing of biotech soybean crops. Law 10,814 was enacted on December 15, 2003 after being approved by Congress, and legalizes the planting and marketing biotech soybean crops for the 2003/2004 harvest. On October 31, 2003, President Lula sent to Congress the long-awaited draft of a Biosecurity Law that will provide a long-term regulatory regime for the biotech sector. The current text of the bill envisions a complicated mechanism for approval of biotech products by a national commission attached to the President's office that would consider political and economic, as well as scientific factors. It is likely that the bill will undergo substantial revision before passage, which is expected in April 2004.

On April 24, 2003 the Brazilian Government published Decree Number 4680, which formally implemented the provisions of a 1990 law (law 8,078 of September 1990) that requires labeling of GMOs. The decree requires labeling of GMOs and products containing GMOs, including meats from animals fed with GMO feed. The label must include a special logo created by the Ministry of Justice in October 2003. The requirement does not apply to packaged food products containing less than one percent of genetically modified organisms.

GOVERNMENT PROCUREMENT

Brazil is not a signatory to the WTO Plurilateral Agreement on Government Procurement, and transparency in the procurement process could be improved. Remaining limitations on foreign capital participation in procurement bids can reportedly impair access for potential service providers in the energy and construction sectors. Brazilian federal, state and municipal governments, as well as related agencies and companies, in general follow a "buy national" policy. Although Law 8666 of 1993, which covers most government procurement other than informatics and telecommunications, requires nondiscriminatory treatment for all bidders regardless of the nationality or origin of product or service, the law's implementing regulations allow consideration of non-price factors giving preferences to certain goods produced in Brazil and stipulating local content requirements for eligibility for fiscal benefits. Decree 1070 of March 1994, which regulates the procurement of information technology goods and services, requires federal agencies and parastatal entities to give preference to locally produced computer products based on a complicated and nontransparent price/technology matrix. However, Brazil permits foreign companies to compete in any procurement-related multilateral development bank loans and opens selected procurements to international tenders.

EXPORT SUBSIDIES

The Government of Brazil offers a variety of tax, tariff, and financing incentives to encourage production for export and the use of Brazilian inputs in exported products. An export credit program known as PROEX was established in 1991. PROEX is intended to equalize domestic and international interest rates for export financing and to directly finance production of tradable goods. Exporters enjoy exemption from withholding tax for remittances overseas for loan payments and marketing, as well as from the financial operations tax for deposit receipts on export products. Several PROEX programs have been found to be countervailable under U.S. law in the context of specific countervailing duty cases. In 1999, a WTO panel found PROEX interest equalization payments used to finance the sale of regional aircraft manufactured in Brazil to be a prohibited export subsidy. The WTO Appellate Body upheld this finding. The Government of Brazil states that it has modified PROEX so as to bring it into conformity with WTO subsidy rules. Canada challenged this position in the WTO, but subsequently reached a negotiated settlement with Brazil, obviating the need for a WTO ruling on the merits of the case. Changes to PROEX were announced most recently in 1999, expanding the program. In 2003, roughly \$808 million was budgeted for PROEX, with \$400 million slated for equalization and \$408 million for direct financing. Actual spending on PROEX during 2003 is expected to have been about half of the amount budgeted.

Patents and Trademarks

Brazil's industrial property law, covering patents and trademarks, took effect in May 1997. The law improved most aspects of Brazil's industrial property regime, providing patent protection for pharmaceutical products and processes, agrochemical products and other inventions. However, concerns continue about a provision that prohibits importation as a means of satisfying the requirement that the patent be "worked" in that country. This issue was the subject of a Dispute Settlement proceeding at the WTO, which was terminated without prejudice in June 2001. The dispute was terminated based on Brazil's commitment to hold talks with the U.S. should it deem necessary in the future to grant a compulsory license for failure to work a patent.

On December 14, 1999, the Brazilian Government issued a Provisional Measure that became Law 10,196 in 2001, which includes some problematic provisions, including a requirement that Health Ministry approval be obtained prior to the issuance of a pharmaceutical patent. This would appear to conflict with Article 27 of the TRIPS Agreement, and U.S. officials have raised this concern with their Brazilian counterparts. "Pipeline" protection is provided for inventions not previously patentable in Brazil because of limitations on patentable subject matter, if these inventions were patented in another country and not marketed in Brazil. While Brazil's patent office, the National Institute for Industrial Property (INPI), is addressing its backlog of both pipeline and regular patent applications, the resources and support necessary to effectively and consistently manage the processing of patent applications still appear to be insufficient. As of December 2003, industry sources reported that INPI had granted fifteen pipeline patents and fifty-seven regularly filed pharmaceutical patents. At the same time, unauthorized copies of pharmaceutical products have received sanitary registrations relying on undisclosed tests and other confidential data, in apparent violation of TRIPS Article 39.3.

Following the WTO agreement on access to medicines in September 2003, President Lula issued a decree revising the implementation of Article 71 of Brazil's 1996 patent law, which governs the granting of compulsory licenses in cases of national emergency or public interest. The decree essentially allows for the importation of copies of medicines from producer countries where patent protection does not exist in cases where local production of the medicine is not feasible. The Brazilian government has yet to make use of the decree, but has publicly stated its intention to do so as a last resort in price negotiations with pharmaceutical companies supplying antiretrovirals to the country's National AIDS Program.

On December 17, 2002, the Brazilian Congress passed Law 10,603 on data confidentiality. The law covers pharmaceuticals for veterinary use, fertilizers, agrotoxins, their components and related products; the law does not cover pharmaceuticals for human use. The law provides data protection for only 10 years from the date of registration with the competent regulatory authority for products utilizing new chemical molecules or new biological organisms or until the first release of the information by the registration owner, with a minimum guaranteed period of protection for one year. For products not utilizing new molecule or organisms, the period of protection is five years or until the first release of information with a one-year minimum period of protection. Data demanded by the regulatory authority after registration will be protected for the duration of the protection period granted to the data used to gain the registration, or for one year after being presented, whichever is longer. If the product is not commercialized within two years of the date of registration, third parties may request use of the data for registration purposes. The regulatory authority may make compulsory use of the data in cases of national emergency or in certain circumstances relating to unfair competition.

The 1997 industrial property law also added provisions for the protection of "well-known" trademarks, but contains a long list of categories of marks that cannot be registered. U.S. industry has expressed concern with the continued high level of counterfeiting in Brazil. A bill (PL_1787) on the protection of layout designs of integrated circuits (required by TRIPS) was introduced in April 1996 and is still progressing through committees within the Brazilian Congress.

Copyrights

A copyright bill that included amendments to bring Brazil into compliance with the Berne Convention and TRIPS was

signed by President Cardoso in February 1998. A software law was signed by President Cardoso that same month, protecting computer programs as "literary works," increasing the term of protection to 50 years, and making software infringement a fiscal and an intellectual property crime. Copyright enforcement in Brazil continues to be uneven, and losses from piracy remain significant. As a result of this concern, on January 10, 2001, the U.S. Government accepted a petition, submitted by the International Intellectual Property Alliance, to review the GSP status of Brazil. This petition was reviewed as part of the 2003 Annual Generalized System of Preferences Product and Country Eligibility Review. A Country Practices Review of Brazil was held in October 2003. The U.S. industry reports that in 2002 its trade losses from copyright piracy in Brazil were over \$771 million, the largest amount of losses due to copyright piracy in the hemisphere.

Problems have been particularly acute with respect to sound recordings and videocassettes, and virtually all audiocassettes sold are pirated copies. Brazil accounts for over half of the market for sound recordings in Latin America and is one of the world's largest markets for videos. Vigorous industry and Brazilian Government anti-piracy campaigns have had a positive impact and general awareness among the populace has increased significantly.

In June 2003, the Brazilian Congress launched a Parliamentary Investigative Commission (CPI) on Piracy, which has gained wide support from industry for its action-oriented nature, as well as its willingness to address the official corruption inherent in piracy. Several Deputies on the CPI have pressed law enforcement officials to achieve notable apprehensions of perpetrators and counterfeited goods ranging from cigarettes to CDs. The CPI's 6-month mandate has recently been extended. An outgrowth of the CPI, a Congressional caucus on piracy and tax evasion was formed in September 2003. Efforts in 2003 resulted in many prosecutions, but the number of convictions for intellectual property rights violations remains too low to act as a deterrent. While anti-piracy actions in 2003 resulted in several large seizures of pirated CDs, the sound recording industry estimates that the piracy rate for CDs in 2002 was 55 percent. Even with piracy raids and more prosecutions, the number of cases prosecuted and sentenced in Brazilian courts remains low, frustrating efforts at deterrence. In July 2003, President Lula signed a law that doubled the minimum penalty for copyright violations. The law also codifies procedures to seize and destroy contraband and gives judges authority to dispose of seized goods to ensure they will not be used for commercial purposes. Brazil has increased inspections at border crossings increased, but significant amounts of pirated material continue to enter Brazil from Paraguay.

The Federal Government of Brazil to date has not given police adequate tools or training to effectively enforce the law. Further, fines provided for in the penal code are too insignificant to create a true deterrent; and the court and judicial process is often unresponsive and slow. The generally inefficient nature of Brazil's courts and judicial system has complicated the enforcement of intellectual property rights. The Brazilian Government is working to streamline the judicial process. In early 2001, the Government created an interagency IPR committee, coordinated by the Ministry of Justice, to improve anti-piracy enforcement. After two years of very limited activity due to lack of resources and the 2002 national elections, the committee made progress in 2003 with a national public awareness campaign and the start of IPR training at the National Federal Police Training Academy. Brazil has not yet ratified the WIPO Treaties on Copyright and Performances and Phonograms.

SERVICES BARRIERS

Telecommunications

Privatization within the telecommunications sector, which is based on the General Telecommunications Law of 1997, has presented regulatory challenges. In the fixed-line sector, interconnection charges and other incumbency advantages have provided strong barriers for entry, and the companies created during a transitional duopoly stage have not fared well. There was also heavy involvement on the judicial side during 2002 and 2003, as some incumbent companies used court injunctions to forestall competition.

Brazil has not yet implemented its original WTO basic telecommunications commitments. In 2001, Brazil withdrew its schedule of commitments in view of concerns raised by certain WTO members that it maintained the right of the Brazilian President to revoke concessions in the case of national emergency, in contravention of the WTO Basic Telecommunications Agreement. This presidential right is contained in Brazil's 1997 General Law on

Telecommunications and is inscribed in Brazil's constitution. Brazil has not sought the constitutional change required to allow a revision of its schedule. Nonetheless, the current regulatory environment generally reflects commitments made by Brazil under the WTO Basic Telecommunications Agreement.

Maritime

The Government of Brazil considers the bilateral Maritime Agreement signed in October 1999 to be expired. Bilateral consultations should result in a new agreement in 2004, and in the interim the regulatory agencies of Brazil and the United States have agreed to continue implementing the provisions of the 1999 agreement on a reciprocal basis. Key provisions of this agreement commit the parties to afford fair and nondiscriminatory access for national-flag carriers and third-flag carriers to competition on commercial cargo and provides equal and nondiscriminatory access to government cargos. A 25 percent merchant marine tax on freight puts U.S. agricultural products at a competitive disadvantage to MERCOSUR products.

Audio Visual Services

Foreign ownership of cable companies is limited to 49 percent. The foreign owner must have a headquarters in Brazil and have had a presence in the country for the prior 10 years. Foreign cable and satellite television operators are subject to an 11 percent remittance tax; however the tax can be avoided if the programmer invests 3 percent of its remittances in co-production of Brazilian audio-visual services. National cable and satellite operators are subject to a fixed title levy on foreign content and foreign advertising released on their channels.

Provisional Measure 2,228 1/01 and later Law 10,454 aim to promote the national film industry through creation of the National Film Agency (ANCINE) and through various regulatory measures. Under Law 10,454, published on May 14, 2002, a fixed title levy is imposed on the release of foreign films in theaters, foreign home entertainment products, and foreign programming for broadcast television. Remittances to foreign producers of audiovisual works are subject to a 25 percent tax. Brazilian distributors of foreign films are subject to a levy equal to an 11 percent tax of their withholding taxes. This tax, called the CONDECINE (Contribution to the Development of a National Film Industry), is waived for the Brazilian distributor if the producer of the foreign audiovisual work agrees to invest an amount equal to 70 percent of the tax on their remittances in co-productions with Brazilian film companies. The CONDECINE tax also levied on any foreign cinematographic or videophonographic advertisement. The fee may vary according to the advertising content and the transmission segment.

Brazil also requires that 100 percent of all films and television shows be printed locally. Importation of color prints for the theatrical and television markets is prohibited. A theatrical screen quota for local films is maintained at 28 days per calendar year. Quotas on domestic titles for home video distributors, while not currently enforced, present another potential hindrance to commerce.

Foreign firms had been prohibited from owning capital in the "open broadcast" (non-cable) television sector. However, in October 2002, President Cardoso issued Provisional Measure 70, which was subsequently approved by the Congress, which permits up to 30 percent foreign ownership in Brazilian media. This law covers print as well as the open television sector. Open television companies also have a regulation requiring that 80 percent of their programming content be domestic in origin. All broadcast media material that enters the country must pass through the Ministry of Justice, which retains rights to censure and edit content.

Express Delivery Services

A bill (PL 1491/99) that would reorganize the National Postal System remains under discussion in the Brazilian Congress. The current proposal creates a regulatory agency for postal services as well as a new Postal Company of Brazil, owned and operated by the federal government. Although the bill would end the government monopoly over postal services after a ten-year period, it would also create a monopoly on the delivery of certain types of correspondence and parcels that are not now subject to regulation, such as express delivery packages, thereby significantly inhibiting market access by U.S. firms.

Insurance

Brazil is potentially South America's largest insurance market, and earnings from premiums have grown rapidly in recent years. In 1996, Brazil eliminated the distinction between foreign and domestic capital, and many major U.S. firms have since entered the market, mainly via joint ventures with established companies. The Brazil Reinsurance Institute (IRB) is a state monopoly. While a 1996 constitutional reform ostensibly abolished the monopoly, private reinsurers have been precluded from operating in Brazil pending the IRB's privatization, which has been delayed indefinitely by a court decision. A 2003 Constitutional amendment allows for the regulation of the reinsurance sector, including market entry. If Brazilian shipping companies wish to obtain foreign hull insurance, they must submit information to IRB demonstrating that the foreign insurance policy is less expensive than that offered by Brazilian insurers. Brazilian importers must obtain cargo insurance from insurance firms resident in Brazil, although the firms may be foreign-owned.

Banking and Other Financial Services

Brazil has not ratified the WTO Financial Services Agreement, formally known as the Fifth Protocol to the GATS, which is necessary to bring Brazil's commitments under the Agreement into force. The Financial Services Agreement is still pending approval in the Brazilian Congress. U.S. service exports to Brazil are impeded by restrictive investment laws, lack of transparency in administrative procedures, legal and administrative restrictions on remittances and sometimes arbitrary application of regulations. Service trade opportunities in some sectors have been affected by limitations on foreign capital participation.

In negotiating the 1997 WTO Financial Services Agreement, Brazil made commitments in almost all service sub-sectors for non-insurance financial services, including banking and securities services. Brazil's constitution precludes the expansion of foreign-owned banks until new financial sector legislation is issued. For practical reasons, new legislation has not been issued, but the President of Brazil has the authority to authorize new foreign participants on a case-by-case basis. In practice, Brazil has approved most plans by foreign service suppliers to enter the market or expand existing operations. As of December 2002, foreign-owned or controlled assets accounted for one third of Brazil's total financial sector equity, and over 18 U.S. financial service suppliers had established significant operations in Brazil.

During 2002, a U.S. company involved in credit bureau activities raised national treatment concerns regarding the refusal by Receita Federal, Brazil's internal revenue service, to provide it with information that was being obtained by its local competitors.

INVESTMENT BARRIERS

In addition to restrictions discussed above, various prohibitions limit foreign investment in internal transportation, public utilities, media and other "strategic industries." Foreign ownership of land adjacent to national borders remains prohibited under Brazilian law, unless approved by the National Security Council. Despite investment restrictions, U.S. and other foreign firms have major investments in Brazil, with the U.S. accounting for more than one third of total foreign investment. There is no Bilateral Investment Treaty between the United States and Brazil.

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